

Why Only Some See Benefit From Fed's Cuts

**Mortgage Rates Remain High
For New Buyers, but Holders
Of ARMs See Lower Resets**

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The Federal Reserve yesterday lowered interest rates for the sixth time since September, but the campaign is helping with only certain kinds of borrowing.

Rates on home-equity lines of credit, credit cards and auto loans have all dropped. In addition, millions of homeowners won't face higher rates as their adjustable-rate mortgages reset.

But for new-home buyers and those looking to refinance their mortgage, the Fed's rate-cutting campaign has provided little relief.

Rates on 30-year mortgages fell to about 5.75% earlier this week, amid anticipation that the Fed would slash its key federal-funds rate by a full percentage point. After the Fed yesterday instead cut rates by three-quarters of a point, rates on 30-year mortgages bounced back to about 6% for some lenders. That's only about a quarter-percentage point lower than in September, even though the fed-funds rate has fallen three percentage points since then.

What's up? Blame the investors who buy packages of mortgages on Wall Street.

Burned by the subprime-lending scandal and a rising level of defaults, these investors, who include pension funds, insurance companies and bond mutual funds, are demanding a greater premium for mortgages over risk-free investments such as U.S. Treasuries. That's a big change from recent years, when investors viewed mortgages as a generally low-risk product.

If the mortgage market were functioning normally, rates would be in the low 5% range for a 30-year mortgage, says Frank Trotter, president of EverBank Direct, which originates mortgages. Mortgage rates typically follow the 10-year Treasury and have historically traded at about 1.8 percentage points above the 10-year Treasury yield. Those Treasuries currently yield about 3.451%.

The best strategy for home buyers: Comparison-shop. Mortgages aren't all priced alike. Some banks keep the mortgages they write on their books; others sell them on Wall Street (as long as investors are buying). And investors' fickleness these days can whipsaw rates.

Buyers should also be willing to act quickly. Daniel Schwartz of Marina del Rey, Calif., took advantage of a brief dip in rates earlier this year and refinanced his 30-year fixed-rate mortgage at 5.125%, down from 5.875%, resulting in a savings of about \$150 to \$200 a month. While the 31-year-old computer analyst was able to "nail" that rate, by the time he told his friends, he says, that rate was gone. "Most people haven't been able to get a good rate on a mortgage even though the Fed has been cutting rates," he says.

Consider how erratic adjustable-rate mortgages have been acting in recent weeks. So-called 5/1 ARMs -- with rates that are set for five years and adjust annually thereafter -- plunged in late-January to 5.26%, down nearly a full percentage point from mid-December. Yesterday morning, however, ARM rates surged to 6.75%. The reason is that "several lenders were liquidating their ARM portfolios to raise cash," says Michael Menatian, president of Sanborn Mortgage Corp., a mortgage bank in West Hartford, Conn. To entice investors, newly issued ARMs must sport higher rates.

Home buyers who can afford higher payments might consider a mortgage with a shorter payment schedule. One of the effects of the current credit crisis is that mortgage investors are keen on buying 15-year mortgages "because they perform better in terms of delinquencies, the borrowers are a better risk, and the mortgages aren't refinanced as quickly," says Mr. Menatian. He says his firm locked in more than 20 mortgages between Monday night and Tuesday afternoon, "and every single one of them was a 15-year."

Even in areas where rates are falling, such as loans tied to the prime rate, the credit crunch is making it tougher for consumers to take advantage.

Rates on home-equity lines of credit have dropped to 6.27% from 8.25% since September of last year, according to Bankrate.com. Partly as a result, the amount that homeowners borrowed against their lines of credit rose slightly in the fourth quarter of 2007 -- the first such rise since early 2005, according to data from Equifax Inc. and Moody's Economy.com. Rates on home-equity lines of credit should fall further after the Fed's latest cuts, but that might have less effect than would ordinarily be expected, as some banks make these loans harder to get.

In recent months, Countrywide Financial Corp., [Washington Mutual](#) Inc., and others have reduced or frozen the amount of credit available to certain borrowers to protect themselves against falling home values and rising delinquencies. Indeed, banks are expected to post a jump in losses from home-equity loans amid a rise in delinquencies. About 4.65% of fixed-rate home-equity loans and 2.01% of home-equity lines were delinquent in the fourth quarter of 2007, up from 3.11% and 1.07%, respectively, a year earlier, according to Equifax and Economy.com.

Indeed, mortgage brokers say their customers are having a harder time borrowing against the equity in their homes. "We're seeing a lot of lenders freezing whatever is outstanding," says Mitch Ohlbaum, a mortgage broker with Legend Mortgage Corp. in Los Angeles. He says some clients, worried about getting cut off from existing lines of credit, have started drawing down their lines in a pre-emptive move.

"They're putting the money into savings accounts and CDs because they're afraid they're going to lose access to the funds," he says. "It's their safety net."

When it comes to credit cards, average rates on variable-rate cards have fallen to 12.36% from 13.97% last fall, according to Bankrate.com. But for some cardholders, yesterday's Fed rate cut may not have as much impact as previous rate cuts because of the presence of so-called floor rates, or predetermined points below which rates won't fall, no matter how low interest rates go, says Greg McBride of Bankrate.com. The last time consumers hit floor rates was between late 2001 and 2003, when interest rates were falling.

A rate cut isn't likely to have a big effect on new-car loans, in part because many auto loans are already offered at reduced rates because of heavy manufacturer incentives. Average rates on five-year new-car loans have dropped to 7.22% from 7.72% in early September, according to Bankrate.com. Nevertheless, lower interest rates will help make it less costly for auto makers and lenders to offer lower-cost loans and more-attractive leasing deals. Already, car makers are sweetening their financing rates, rebates and lease deals on a wider range of models than usual.